

Regulatory Commission Issues and Role in Regional Transmission Entity Governance

***Preliminary Note:** Although an early draft of this paper was made available to the RRG governance work group early on Monday, October 20, the work group ran out of time at its Tuesday, October 21 meeting and did not have an opportunity to review or discuss this paper.*

Introduction

The purpose of this paper is to initiate a discussion about the role of utility regulatory commissions in the governance and the regulation of any new entity or contractual arrangement (jointly referred to as “entity”) formed for the purpose of managing various transmission system functions in the “RTO-West Footprint” region (“Region”). The term “regulatory commission” is intended to include State, Provincial and Tribal regulatory commissions to the degree those commissions have regulatory obligations regarding rates and service to retail customers that are substantially the same or similar to those of the state commissions.

The paper focuses on concepts and framework, rather than the specific details of individual state or FERC legal requirements. Those details will necessarily depend on the actual structure of any new entity, and particularly on the functions to be performed under that structure. A key, but as yet unanswered question, is the jurisdictional status of these various functions if they are taken on by a new entity. That jurisdictional status will determine where ultimate decision-making authority lies: with the states and other governments in the region, or with the FERC.

Assuming a state jurisdictional nexus, the obvious threshold issue for state regulators will be whether to approve the participation of state-jurisdictional utilities in a new regional entity. Those decisions will depend on the functions the entity is to perform, their costs and benefits, and any other matter that falls within the jurisdiction of the particular state commission to grant such approval.

Assuming that these threshold approvals are obtained, and an entity is formed, this paper focuses primarily on the regulatory dimension of the independence and governance of that entity, rather than on the corporate governance structure itself. However, some of the ideas we describe touch on the possibility of interaction between corporate governance and local¹ government regulation, particularly to achieve information exchange and regional accountability for any new institution.

The goal of the paper is to suggest some ways to fulfill necessary regulatory obligations and preserve accountability in the Region, while at the same time facilitating the formation of new institutional solutions for transmission system problems and opportunities if those

¹ The use of the term “local” is generally a reference to state, provincial, and tribal regulatory authority oversight. However, in some contexts, such as in a planning context where siting decisions may be implicated, coordination with other “local” entities may be appropriate. Some examples of such a situation include siting across federal or military lands, siting within a city boundary where the utility is not state regulated, siting on an Indian reservation where the tribe does not have a regulatory commission, and certain Canadian or cross-border matters.

solutions are determined to be cost-effective and beneficial for the Region's retail electricity customers.

The intended audience for the paper includes both the RTO West RRG and the various state commissions whose jurisdictions are included within the Region.

Regulatory Context

Generally, state regulatory commissions are obligated under state laws to regulate in the public interest the rates, terms, and conditions for service provided to retail electricity customers by utilities under state commission jurisdiction. State laws in the Region vary in the way this regulatory obligation is defined. Whatever the obligations are for each state, a state commission cannot delegate its jurisdiction or its obligations to a third party, unless authorized by state law to do so. We are not aware of any state law within the Region that provides any such authorization for a state commission.

Canadian Provinces have regulatory bodies with authority over matters of retail service and rates that is similar to utility commissions in the states. [more detailed information from the Canadian regulators is necessary to define this aspect of the regulatory context].

Indian Tribes have regulatory jurisdiction over tribal trust lands and other related authorities over other lands within Indian reservations.²

The FERC is obligated under federal law to regulate utility rates, terms, and conditions of service that fall under its jurisdiction. The FERC cannot delegate its jurisdiction or its obligations to a third party, unless authorized by federal law to do so.

The transmission and related service issues under discussion by the RRG implicate some matters that fall within state and local jurisdiction, and some that fall within federal jurisdiction. Also, the nature of the Region being what it is, a substantial proportion of transmission and related services are provided by utilities that do not fall within the jurisdiction of either state commissions or the FERC.

RRG discussions have touched on a number of matters that fall within the traditional concerns of the jurisdiction of states, provinces and tribes and therefore trigger local legal obligations. Examples of existing state regulatory interests include: the transmission capacity necessary for reliable bundled retail service; assignment of operational control of utility transmission and other facilities to a new entity; the recovery of and on existing transmission investment in retail ratebase; availability of wheeling revenue to credit against retail revenue requirement; recovery of costs for new transmission investment; short-term and long-term system adequacy for utilities to fulfill service obligations; and the costs and risks incurred by utilities under either cost-based or market-based systems to serve retail customers.

If a new structure for transmission management encompasses matters that fall within state jurisdiction, it will necessarily implicate some level of local regulatory obligation

² At this time very few tribes have authorized bodies that regulate electricity, however during the term of a potential RTO such bodies could be formed or other methods for exercise of this authority may be created.

regardless of whether the new structure is a system of contracts, or a new independently governed institution.

In addition to the obligations of regulatory commissions that relate to the regulated retail utilities, states, provinces and tribal decision makers are implicated by other transmission related issues. These decisions involve siting of new facilities, taxation authority over certain transmission functions, and oversight of environmental and cultural resource related impacts of transmission construction and operation of the electric power system.³

Relationship of Local Regulatory Obligation to Corporate Structure

The formation of a new regional transmission entity, whether independently governed or not, does not change regulatory jurisdiction or obligations for the states, provinces, tribes, or FERC. It may change the way those obligations are fulfilled, but it does not change the fact that they exist.

Including the commissions—or FERC, for that matter—as a *stakeholder* in the governance structure of a transmission entity can serve to elicit policy input for the entity, but it does not and cannot serve to fulfill either the state commissions' or FERC's legal obligations. This is simply because those obligations cannot be delegated to the decision-making of a stakeholder committee or to the Board of a new entity—particularly an entity that provides utility services that are fundamentally jurisdictional to the local governments or to FERC, or both.

The governance structure proposed by RTO West is an example of this kind of “stakeholder” role for states, provinces and tribes. The governance structure approved by FERC as consistent with Order 2000 provided for utility commission participation in two ways: 1) as members of the self-selected Stakeholder Advisory Committee; and 2) State and Provincial Energy Authority⁴ election of 4 voting members of Class 5 and election of one voting member by Tribal Utility Regulatory Authorities out of the total 30-member Board of Trustee Selection Committee. In both cases, the commission role is one of a stakeholder within the membership classes and sub-classes. Again, this may well be beneficial to the regulators in the region and to the entity (in this case, RTO West) for policy input. But participation in the selection of the Board of RTO West does not serve to extinguish whatever obligations the regulators have with respect to services provided by *members* of RTO West who are also state or otherwise regulated, or actions of the Board itself, if any of *its* actions fall directly or indirectly within the jurisdiction of the regulators.

Similarly, if the Region pursues a contract-based approach to transmission management, allowing the regulators to be contract signatories does not serve to extinguish their obligation to regulate the services provided by utilities who are also contract signers.

³ States, provinces and tribes may also initiate and participate in dispute resolution proceedings related to these issues. However, such participation will be carefully considered as an addition to other legal regulatory obligations that can not be delegated. Disputes can often be avoided when all parties participate in advance in information sharing and decision making processes.

⁴ An Energy Authority is actually defined more broadly than a regulatory authority.

Our point here is not to criticize the governance structure proposed by RTO West, or the contract coordination approach proposed by others. Rather it is to emphasize that the regulatory obligations of governments in the Region are separate and apart from whatever role the regulatory commissions might play in advising or participating in governance structures. Fear of compromising the objectivity of regulatory decisions is, indeed, a key reason why state commissions have been cautious and generally unwilling to participate substantively in those governance structures.

The State Interest in Accountability within the Region

Because of the fundamental issues of jurisdiction and regulatory obligation, the state and other regulators in the Region have all shown a strong interest in ensuring that any new transmission arrangements implemented in the Region are designed to solve the Region's problems and capitalize on the Region's opportunities.

Although RTOs are creatures created by FERC in Order No. 2000, FERC has not taken an active role in oversight or review of RTO operations and/or governance once RTOs are operational. FERC's tendency, aided and abetted by the RTOs themselves, has been to rubber-stamp any changes to RTO tariffs filed by RTOs, regardless of the ramifications of such changes. Although existing RTOs have filed some significant organizational changes with FERC that have garnered a great deal of attention, RTOs are routinely filing significant policy decisions using the RTO tariff as the vehicle for such changes. (It is unclear how, or even if, these changes are being authorized by RTO staff and/or RTO Boards.)

While FERC remains legally responsible for regulatory oversight of the transmission services provided by RTOs or other similar structures that fall within its jurisdiction, these entities have clearly taken on growing responsibilities for electricity markets within their respective regions. However, FERC has no accountability beyond its statutory obligation to see that transmission service is offered in a nondiscriminatory manner at just and reasonable rates and that wholesale electricity markets result in just and reasonable rates. Thus, it is incumbent on the state and other governments in the RTO West footprint to fashion a role that results in oversight and that holds the RTO or similar structure accountable for its impact within the region. Absent such a role for the regulators in the Region, they are reduced to being complainants or intervenors at FERC whenever tariff changes are filed, or whenever the impact of actions by RTOs or similar structures, get out of hand.

Further, FERC has never clearly delineated how the operations of RTOs should be reviewed and evaluated, or how the plans of action of RTOs should be implemented, primarily because FERC has not exercised this oversight of RTO operations and FERC lacks jurisdiction regarding transmission planning and expansion because these areas are state jurisdictional. Thus, FERC's track record has been to set RTOs in motion, but not hold them accountable, other than in a cursory manner.

As a result of this situation, the states, provinces and interested tribes in the RTO West footprint should periodically review and evaluate the operations of the grid management entity/contracts/RTO that fall within FERC's jurisdiction to determine whether such entity is meeting the grid management goals of the region. This oversight by the state regulators

and government decision-makers should be coordinated with the Board of any such entity. To ensure further accountability, the appropriate government bodies in the Region should play an active role in the review of planning and expansion functions because the results of these plans will ultimately come under their review. A final necessity for the states would be oversight of tariff changes before they are filed with FERC for approval to determine how such changes will impact the region. It would seem logical that such tariff changes should be formally approved by the Board with input from stakeholders, so that by the time they get to the state and other regulators for review, the policy implications will have been thoroughly aired within the RTO or similar organization.

Options for Regulatory Commission Role

Given that the regulatory role is generally separate and apart from the governance of regional transmission, how can the regulators in the Region play a role that is both constructive for regional actions that promise regional benefits, and effective for fulfilling regulatory obligations?

We have organized some ideas around a set of objectives.

Objective Number 1: Coordinate the exercise of regulatory commission jurisdiction to support regional action.

A **regulatory commission coordinating committee** would address this objective by providing a forum to coordinate regulatory decisions that fall within local-level jurisdiction in the aid of regional problem-solving. Since regulatory commissions cannot delegate their authorities and responsibilities, such a committee could not make decisions that would be binding on the commission members. But the existence of a forum for coordination would ensure that decisions were informed with a regional perspective.

The purpose of this committee would be to help coordinate the actions of local agencies with substantive regulatory authority. Consequently, its membership would be limited to such agencies and it would not be a broad-based, stakeholder-populated committee.

Objective Number 2: Provide a channel for advice to the decision-makers in the transmission entity from regulatory commissions in the Region.

A **regulatory commission coordinating committee** would also provide a forum for advice to the management decisions of the transmission entity regarding matters that fall within regulatory commission jurisdiction. Moreover, it could provide a forum and channel for advice from regulators in the region regarding actions and decisions of the entity that fall within FERC's jurisdiction (see Objective 4, below).

Objective Number 3: Provide for regulatory commission input to the governance structure of the transmission system entity.

The objective here is to provide for regional policy input and participation in the actual governance of the entity. The RTO West proposal provides for participation of states and other governmental bodies in membership class 5. Our understanding is that this membership would not be limited to regulatory commissions (i.e., it could include energy

offices, siting agencies, etc.). This proposal works for purposes of generally including regional input to the governance structure.

Objective Number 4: Preserve accountability within the Region.

Regardless of the ultimate structure of the transmission entity, it is likely that a number of its functions will be FERC-jurisdictional, or could evolve to become FERC jurisdictional. The entity will necessarily have the authority and the obligation to make FERC filings. Decisions with respect to those filings could benefit from the views of the Region's regulators. At this point, we can see two formal ways that those views might be included in the entity's decisions with respect to FERC filings⁵.

- 1) As a formal requirement to consult with the committee described in Objective 1, above.
- 2) As a formal requirement to secure affirmative approval of the committee described in Objective 1, above.

The consultative role is the more practical. Formal approval would require that the committee be constituted with formal decision-making processes that might prove difficult to establish. The consultative role, though non-binding, would certainly send a message to the entity and lay the groundwork for any necessary political or FERC-process action should the entity chose a course of action inimical to the Region's interests.

Objective Number 5: Provide coordination between FERC-jurisdictional decisions and the regional perspectives of the Region's regulators.

FERC cannot delegate its regulatory obligations to a regional body (without authorization in federal law to do so) any more than state regulators can delegate their authorities. However, the Federal Power Act does provide an administrative mechanism for FERC to include the participation of state regulators in its formal decision-making. The FERC is authorized to refer matters under its jurisdiction to "joint-boards" that may include FERC commissioners as well as state commissioners⁶. *Section 209 Federal Power Act*. The use of this mechanism for addressing regional (multi-state) transmission issues that fall within FERC's jurisdiction is not well-tested. This may well be an area ripe for further exploration.

⁵ Under the current governance structure, FERC filings are required by the Bylaws to be submitted to the Board Advisory Committee for review. If this structure is maintained, another possibility is affording the regulatory representatives the opportunity to take concerns they have to the Board. Other proposals now under discussion in the governance work group may allow for vetos or affirmative approvals of certain changes to the decided status-quo structure. The ultimate governance structure should be considered for inclusion of the role of regulators consistent with the concerns expressed in this paper.

⁶ FERC has adopted a new policy for Government-to-Government consultation and coordination with Indian Tribes. While the Act does not specifically mention Indian Tribes, Interested Tribes may be included in such a body under authority of the new policy. [Add statement on how Provinces may be included in participation.]